

**Testimony of Mr. Michael R. Gorham**  
**President of the National Propane Gas Association**  
**Before the Subcommittee on Conservation, Credit,**  
**Rural Development, and Research**  
**Of the House Committee on Agriculture**  
**April 25, 2001**

Thank you for this opportunity to present testimony concerning energy supply and demand issues and their effects on the agricultural sector of our economy. I am Michael Gorham, president of Northwest Gas, a small retail propane business located in Grand Rapids, Minnesota. I appear before you today in my capacity as the President of the National Propane Gas Association.

NPGA is the national trade association of the propane gas industry. The membership of NPGA consists of approximately 3,800 companies and includes 40 affiliated state and regional associations representing members in all 50 states. While the single largest group of NPGA members is made up of retail marketers of propane, the membership also includes propane producers, transporters and wholesalers, as well as manufacturers and distributors of associated equipment, containers and appliances.

Our members operate in nearly every one of the 435 congressional districts in the country. In fact, there are approximately 641 retail propane marketers located in the 15 districts represented by members of this subcommittee.

### **Propane Production and Consumption**

Approximately 60 million consumers use propane for agricultural, residential, and industrial heating, cooking and water heating. Propane is also widely used as a petrochemical feedstock and as a clean-burning alternative engine fuel.

Nearly 19 billion gallons of propane are consumed each year in the United States. More than 90% of this volume is produced domestically. Of the relatively small percentage of product that is imported, approximately three-fourths comes from stable sources in Canada.

### **Propane and Agriculture**

Mr. Chairman, we understand that rural America provides the raw materials for our nation's economy. Food, fuel, minerals and forest products are all essential commodities that the American economy cannot do without. NPGA members are mindful of this fact because our industry largely grew up in rural America. For nearly a century, propane has played an essential role in the rural economy because it is versatile, portable and clean burning.

Propane's importance to the U.S. rural economy is demonstrated by the fact that over 30 percent of rural households use our product, according to the 1997 Residential Energy Consumption

Survey by the Department of Energy. This study also reports that about 20 percent of rural households use propane as their primary heating fuel.

For decades propane has also been the preferred fuel for numerous agricultural applications like crop drying, animal brooding and flame cultivation. Mindful of the importance of agricultural markets, in 1996 our industry established the Propane Education and Research Council, which mandates a minimum level of funding for agricultural-related projects. This self-funded research and development program was created in part to develop cleaner and more efficient fuel use equipment for our nation's farms and other businesses.

While research and development advances will lower costs in the future, I understand that the concerns recently expressed by many farmers relate to present-day costs. I am also aware that those concerns are even more pronounced in situations where farmers must adhere to contracts that do not allow unforeseen costs, like rising fuel prices, to be passed on to the consumer.

Many members of our association offer price-hedging programs that are designed to address these concerns. In my view, these programs need to be encouraged. Indeed, there is evidence that progress is being made in this regard. I would like to submit for the record a copy of an article that appeared in Neighbors, the Alabama Farmers Federation magazine. It discusses how some poultry farmers managed to insulate themselves from the full effect of rising costs by taking advantage of hedging opportunities.

## **Factors Affecting Price and Supply**

***Costlier Inputs*** -- Any discussion of propane prices must begin with the understanding that propane is a by-product of crude oil refining and natural gas processing. As such, the wholesale price of propane generally follows the price of crude oil and natural gas. Higher crude and natural gas prices naturally mean higher propane prices.

The committee should note that just over two years ago, the price of crude was a mere \$11 per barrel. Last summer, crude prices reached the \$35 level. Similarly, natural gas prices increased significantly from 1999 average prices of \$2.50 to \$3.50 per MCF to as much as \$10.00 per MCF in December 2000. A report issued in February 2001 by the respected international energy consulting firm of Purvin & Gertz, Houston, TX, found that “natural gas prices in December were more than three times higher than average.”

***Production Disincentives*** – High natural gas prices during this past winter also had a detrimental effect on the supply of propane by creating an incentive not to produce propane. Put another way, higher value natural gas (per BTU) created a market incentive to leave a greater percentage of gas liquids (propane among them) in the gas stream. Some experts have estimated that this practice resulted in a 30% to 50% reduction in normal gas plant production of propane. Such a significant reduction in production had an adverse effect on the price of our product.

***Refinery Fuel Switching*** – During this same winter period, higher than normal natural gas prices also caused petroleum refiners to switch from natural gas to propane to fuel their own refineries. Refinery use of propane, which otherwise would have been sold to retail propane marketers, had

the effect of removing thousands of barrels per day of propane from retail markets. Once again, this drop in the volume of product available for retail markets caused fuel prices to increase.

***Lower Inventory Levels*** – In February 1999, propane stocks were at a surplus level due largely to the mild winter experienced that year. Prices were also at a low level as crude oil prices averaged \$11 per barrel. This attracted major purchasers from the petrochemical sector who purchased significant volumes of propane throughout the balance of that year. These large volume purchases, compounded by an end-of-season blast of severe weather, resulted in propane inventories dropping to record low levels in early 2000. By the end of March 2000, U.S. inventories were below the normal range for that time of year. As of August 31, 2000, propane stocks were able to rebuild to an estimated 59.2 million barrels. While this level is near the lower limit of the normal range for that time of year, it still reflected a 5.5% decrease from the previous year.

***Colder Weather*** – Finally, Mr. Chairman, we should also acknowledge the effect that weather had on fuel bills last winter. Prior to the most recent winter heating season, the U.S. experienced some of the warmest winters on record. Three consecutive warmer-than-normal winters gave most energy consumers a break through lower fuel bills. That trend came to an end late last year when most of the nation experienced normal or cooler-than-normal winter temperatures. According to the National Climate Data Center, the 2000/2001 season was the 14<sup>th</sup> coldest winter in the last 106 years. This stands in stark contrast to the previous 1999/2000 heating season, which was the warmest in 25 years.

We urge the committee to note that these factors have something in common: They are all beyond the control of retail fuel distributors.

### **Factors Affecting Distribution Efficiency**

Mr. Chairman, there are additional factors that affect the ability of retail fuel distributors to reliably serve agricultural users. Some issues involve the government, while others are predominantly private-sector matters. NPGA is committed to working with Congress, Federal agencies and non-governmental organizations to alleviate conditions which contribute to product distribution bottlenecks. We recently constituted a task force made up of producers, transporters and retail distributors. The mission of this task force is to identify realistic, achievable solutions to key distribution impediments. For example,

***Enhanced Fuel Storage Capacity*** – Discussions of federal energy policy are often polarized by the conservation-versus-production paradigm. In our view, too little attention is given to the vast area in the middle -- the distribution infrastructure that takes energy from the point of production to the end user. We believe that consumers would be better served if government provided an incentive to stimulate investment in additional fuel storage capacity.

***Federal Hours of Service Regulations*** –Hours of Service rules restrict, on a daily and weekly basis, the number of hours that drivers may drive and be on-duty. NPGA strongly supports awareness of driver fatigue issues, but reminds Congress that additional flexibility is needed in order to ensure efficient delivery during the peak winter heating season.

Winter 2000/2001 provides an excellent example of how government policymakers already recognize the need for flexibility. Both federal and state agencies traditionally extend relief from the HOS regulations during periods of bad weather, because challenging driving conditions often accompany the winter heating season. But for the first time, state governments extended relief from the HOS regulations for supply-related reasons. Regulators understood that drivers needed to travel greater distances to obtain supplies for their customers and extended appropriate relief. Federal regulators also played a useful role this past winter by clarifying interstate responsibilities in a timely fashion.

Finally, NPGA encourages DOT to allow flexibility from the rigid weekly maximum driving hours provision. Currently, if a driver exhausts his allowable hours of service early in a week, he may not drive until the beginning of the next work week, which can mean as much as 72 hours of lost time. This is a severe burden to propane marketers during the busy winter heating season. DOT should allow companies to return their drivers to their trucks after having rested them for at least 32 consecutive hours. Such a flexible approach has already been proposed by DOT in the form of a fuel oil pilot program, which NPGA strongly believes should also apply to propane. This approach would allow drivers to stay on the road more consistently, thereby ensuring more stable delivery of propane in the winter.

***Jones Act Reform*** – The Jones Act (Merchant Marine Act of 1920) currently prohibits foreign flagged vessels from transporting cargo between U.S. ports. While we respect the preference for domestic carriers, exceptions should be made in cases where rigid adherence to the Act could result in distribution bottlenecks. The Act currently provides for one-time emergency

exemptions, but the process for securing waivers is often cumbersome and invariably untimely. We believe Congress should amend the Jones act to provide a seasonal exemption for propane and other heating fuels.

***Pipeline Consistency*** -- By their nature, pipelines are bottlenecks in the system. Throughout most of the winter heating season, product demand exceeds pipeline throughput capacity. When this occurs, pipelines implement product allocation procedures. Shippers are awarded allocation credits based on historic use. Unfortunately, in the opinion of many NPGA members, pipeline allocation policies have been inconsistent and have taken on the appearance of being arbitrary.

We are working closely with several pipeline companies that serve our industry to ensure that allocation procedures are fair, consistent and publicly accessible. If necessary, we will consider petitioning the involvement of the Federal Energy Regulatory Commission (FERC) to achieve this outcome.

***Expedited Rail Shipments*** – Delays in propane rail shipments have become increasingly problematic. Some shippers have reported a three-fold increase in average shipping times. Whether these delays are the result of recent consolidations in the railroad industry or merely coincidental occurrences is unclear. Nevertheless, NPGA is anxious to begin a dialogue with the Federal Railroad Administration and the railroad industry to explore options for encouraging expedited rail shipments during the winter heating season.

Through the deliberations of our infrastructure task force, NPGA is also exploring the feasibility of temporary, rather than the more costly permanent, rail car offloading facilities.

***Petrochemical Inventory Disclosure*** – The petrochemical industry is by far the largest user of LP-gas, consuming 43% of the propane produced in the country. Petrochemical companies, which maintain large inventories, are not always the end users of the full volume of product which they have acquired. Instead, decisions are often made to reintroduce product back into the retail marketplace based on market factors (e.g. price). This process of shifting huge volumes from publicly disclosed storage to non-disclosed private storage, and then back again, fosters confusion and uncertainty in the marketplace. We urge Congress to promote greater market stability by requiring public disclosure of petrochemical inventories.

***Federal Data Collection*** – Brisk competition in retail markets creates a strong incentive for marketers to arrange for adequate supplies to serve their customers. The availability of accurate and timely inventory data allows marketers to make informed judgments. We encourage Congress to support the Energy Information Administration's data collection program through the congressional appropriations process.

### **History of Federal Intervention**

From time to time, policy proposals surface which call for increasing the role of the federal government in energy markets. History suggests that good intentions often have harmful consequences. Our resistance to enhanced federal involvement is driven by our experience with past attempts at federal intervention.

The propane gas industry was the first to be subjected to mandatory price and allocation control measures of the 1970s. It was also the last industry to be deregulated, an event that did not occur until 1980. During the four-year period from 1974 through 1978, 642 retail propane marketers went out of business. In this instance, federal interference only served to lessen competition and restrict the freedom of consumers to choose an energy provider.

### **Conclusion**

Propane and agriculture are interdependent industries. Both are affected by the supply and demand issues that ultimately determine fuel prices. While neither propane marketers, nor their farm customers can control these issues, there are several areas that are within our reach where we can work together to improve the efficiency of the current fuel distribution system. The members of NPGA are committed to working with Congress and our agricultural customers to address these issues of mutual interest.

On behalf of the members of the National Propane Gas Association, I would like to thank you Mr. Chairman, and the members of the Subcommittee for giving us this opportunity to present testimony this afternoon.